RAVI GUPTA & SONYA HUANG

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Extending Your Runway

Agenda

1. Runway reality
2. How much runway do you need?
3. How to extend your runway
4. Questions and open discussion

- This presentation will cover three main topics:
    - First: What is your runway right now? How should you calculate it?
    - Second: How should you think about how much runway you actually need?
    - Third: How do you actually extend your runway if you need more?
- Our point of view is that most founders need more than they think they do right now.
- One caveat: These are general principles. If you need more tactical advice specifically tailored to your company, your Sequoia board member and your community of founders are ready to help.

Runway Reality

- First, the basics: What is runway?
- It’s your cash balance divided by your monthly burn.
    - If you have $10M in cash and $0.5M in burn, you have 20 months of runway.

- But it gets a little more nuanced than that.
- The cleanest way to look at your cash balance is *net* cash, which is the cash you have on your balance sheet minus any debt you've drawn.
    - If you have $10M in cash but you've drawn $5M in venture debt, you really have $5M of net cash and you should use that number to think about your runway.
- We often get asked why. The reason is that debt is borrowed money. It's not yours. You owe it to a creditor. Similar to how you make personal budget decisions based on your assets minus whatever debt you owe, you should think about your company's cash position the same way.
    - We could dedicate an entire session to the tradeoffs of venture debt. The TLDR is that having a line is a helpful lifeline when you're facing a cash crunch, but drawing it comes at a cost. It makes it harder to raise your next round. It comes with covenants that means debt holders can own more and more of your company. It can be a negative signal, and it can generate a lot of overhang.
    - That said, one of our recommendations if you are tight on cash is to secure a venture debt line and just not to consider it part of your runway. Ideally you don't draw on it unless absolutely necessary, with eyes wide open to the tradeoffs.

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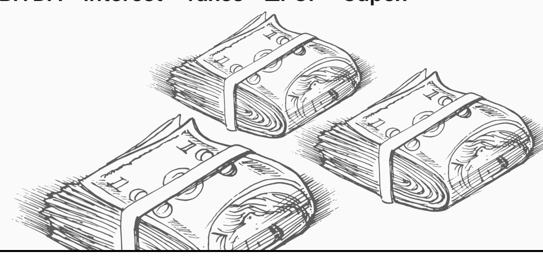
WHAT IS RUNWAY?

Cash balance ÷ monthly burn

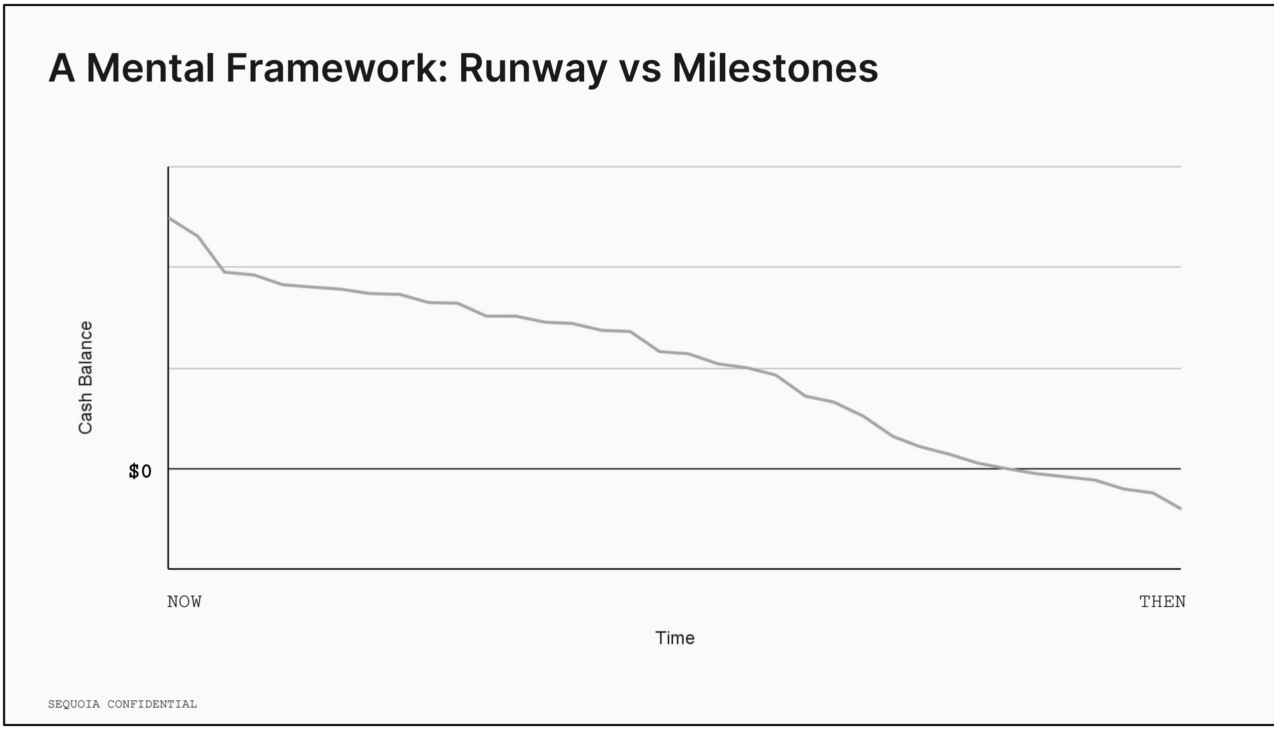
NET cash (cash - debt)

Operating FCF =
EBITDA - Interest - Taxes - ΔFCF - Capex



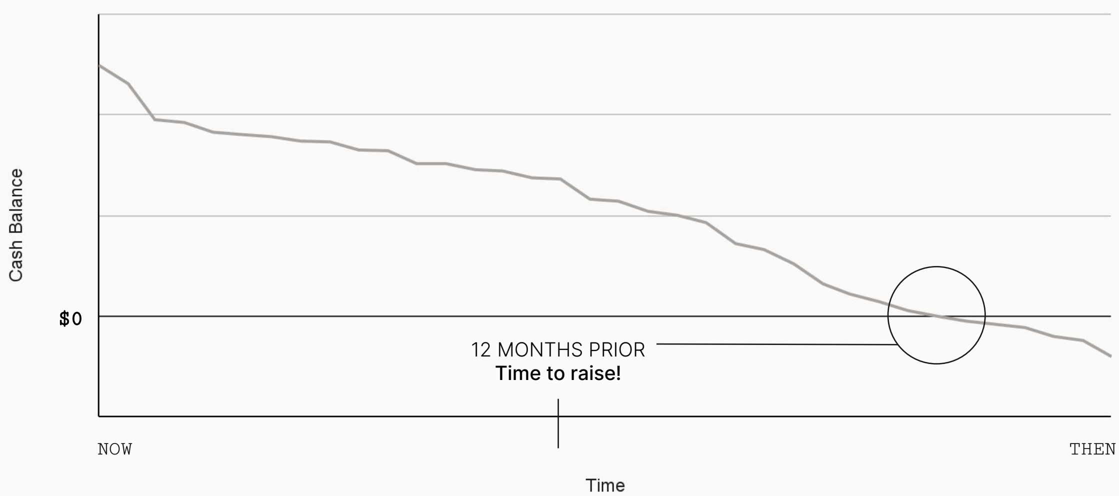
- Monthly burn—this is different from your net income. Net income is an accounting concept. Burn is literally cash in minus cash out.
- It takes into account things that aren’t in your monthly P&L: for example if you have to buy inventory upfront, or if you have capex outlays upfront, or for a subscription company if you collect upfront on yearly contracts—all of these things impact your cash burn.
- It’s critical to have a very tight grip on what your cash burn is. There may be ways to reduce the gap between EBIT and free cash flow—maybe that means paying your suppliers a little later, or collecting revenue earlier.
- If you have a lumpy business, meaning you have to provide cash upfront to build out capital expenditures or you’re purchasing inventory, it’s existentially important to have a very detailed understanding of your expected cash outlays. If you’re not careful in managing and forecasting around these outlier expenses, then your runway can turn out to be 3 months when you thought it was 15.

- One more thing: Runway is not static. Just because you have 8 years of runway doesn't mean you can forget about it and assume you're fine. As your revenue and expense base change, your runway can change very quickly.
- You want to stay focused on the burn number. You should be calculating your runway every single month and watching that number religiously.



- How might this look in practice?
- Suppose you and your CFO put your heads together, and your best guess for how cash changes over time looks something like this chart.

A Mental Framework: Runway vs Milestones



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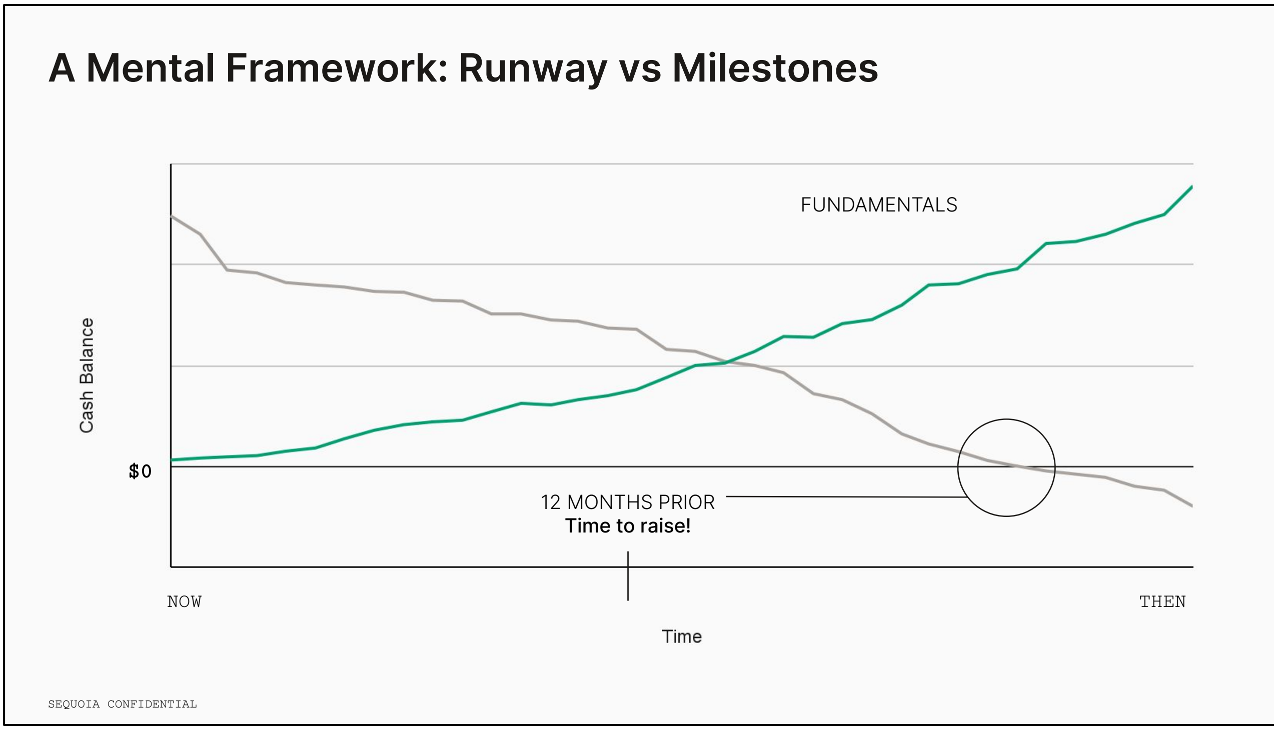
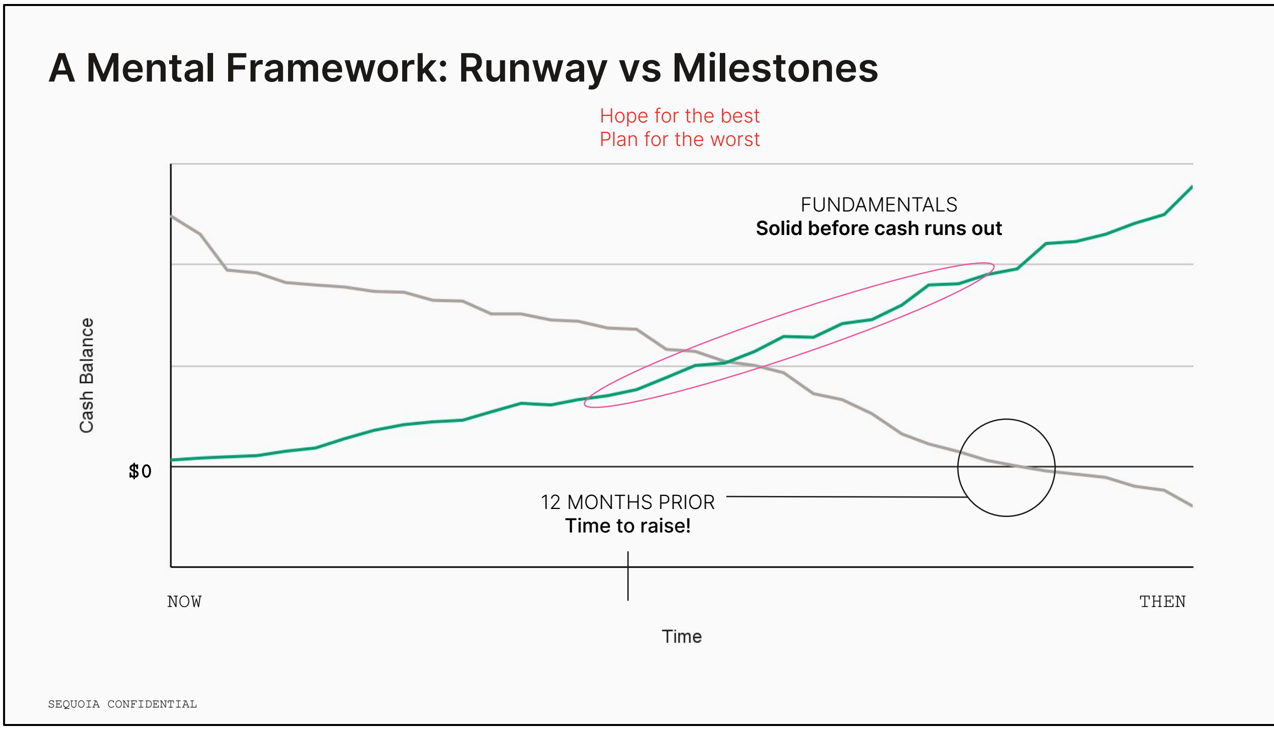
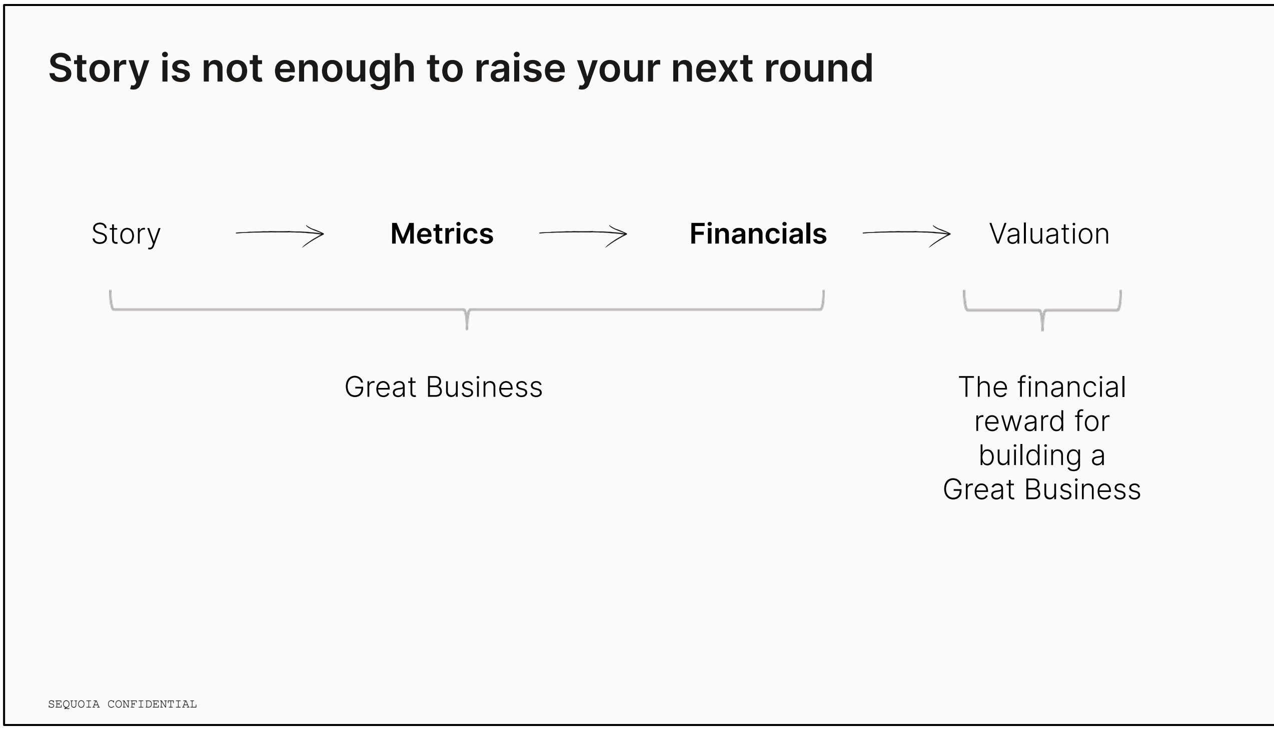
- This is your cash-out point.
- 12 months before that, it’s time to think about raising again.



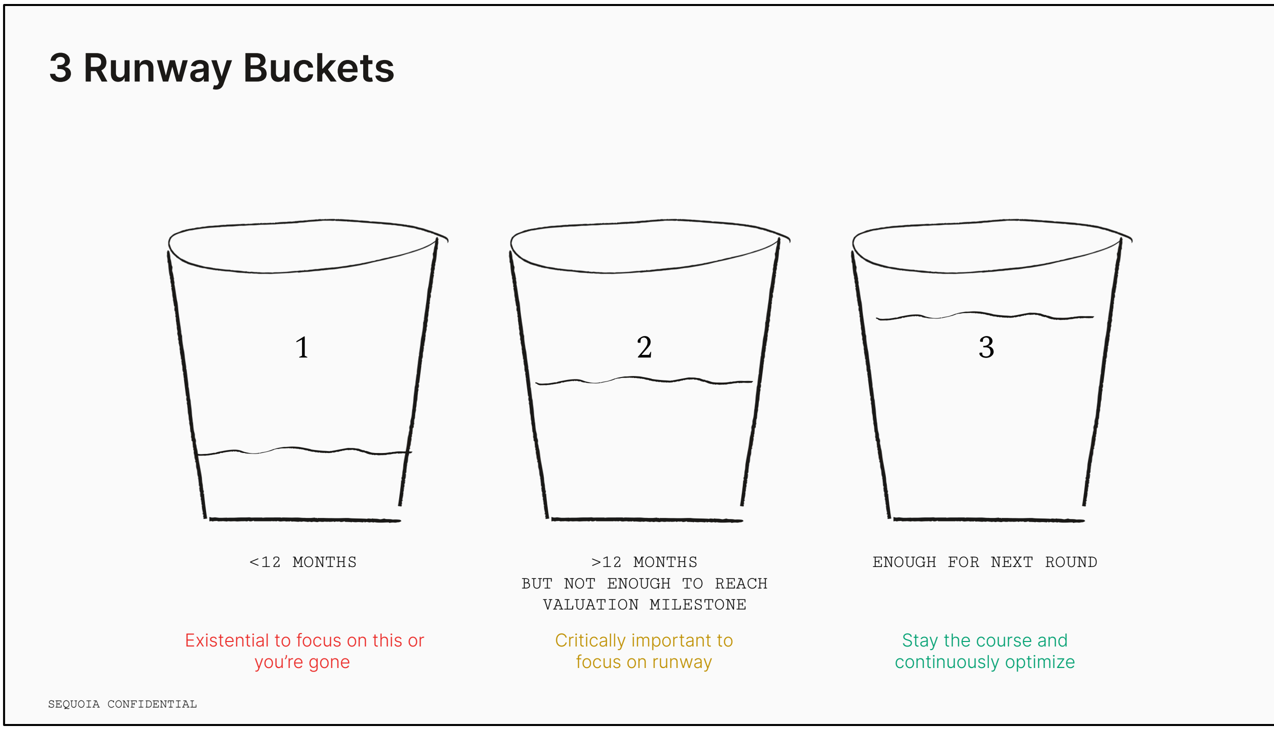
- Runway doesn’t come in a vacuum. It’s intimately tied to meeting valuation milestones.
  - Imagine you’re driving your car on the freeway and running out of gas. What matters is not how many gallons of gas you have in your car, but whether it’s going to last you until you reach the next gas station.
- Think about what your goal is for your next fundraising. Maybe it’s an up round. Maybe it’s a flat round. Maybe it’s a down round. Maybe it’s to reach cash flow positive.
- Whatever your goal is, which is a conversation between the leadership team and the board, there is some valuation milestone attached to achieving that goal.
- Figure out what metrics or “fundamentals” get to you to your goal. Maybe it’s ARR. Maybe it’s Gross Profit. This is the green line on this chart.



- The rough mental framework is that well before you run out of cash, you need to make sure you have the fundamentals in order to meet your next valuation milestone.
- These two lines are intertwined. There's a delicate balance in your scenario analysis between investing in growth and burning cash in order to make sure that you are leaving enough runway to meet the next milestone.
- It's important to hope for the best but plan for the worst as you are plotting out how to make the math work.



- Raising your next round on pure story is not enough anymore. That worked when capital was plenty, but investors are now going to care about your metrics, and more importantly your financials.
- So it’s important to make sure that you are focused on getting that valuation milestone to the right place.



- Now, you've done the exercise of figuring out your runway versus your metrics and valuation fundamentals.
- There are three possible scenarios for your runway situation:
    1. Bucket 1: <12 months of runway, when it is existential to focus on your runway
    2. Bucket 2: 12 months of runway but not enough to raise a flat round based on rational metrics: Here it's critically important to focus on runway.
    3. Bucket 3: Enough runway to raise a flat round, up round or reach cash flow positive: Stay the course and continuously optimize.
- Some founders today are in Bucket 1. A few are in Bucket 3. But many are in Bucket 2.
- If we can emphasize one point in this presentation it's this: **many founders may think they're in Bucket 3, but are actually in Bucket 2.**
- The financials that you have to reach in order to cover your next round have changed. The bar has been raised.
- Many of us are 3-4 years away from reaching our last valuation, with less than that amount of cash. In that case, it's critically important to focus on managing runway, even if you have years of runway remaining.
- Next, we'll cover how to extend your runway.

- If you take us at our word that we all probably need more runway than we thought, the question is: How do you get it?

How to reduce burn and extend runway

1. Understand where you are
2. Lay out the potential changes based on burn impact and ease of execution
3. Set a goal
4. Execute on this goal

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- Like many things in business, it's very easy to say and it's very hard to do.

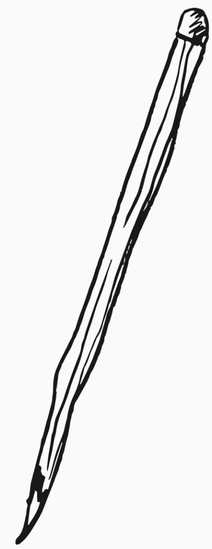
1. Understand where you are

Understand where the money goes in your P&L

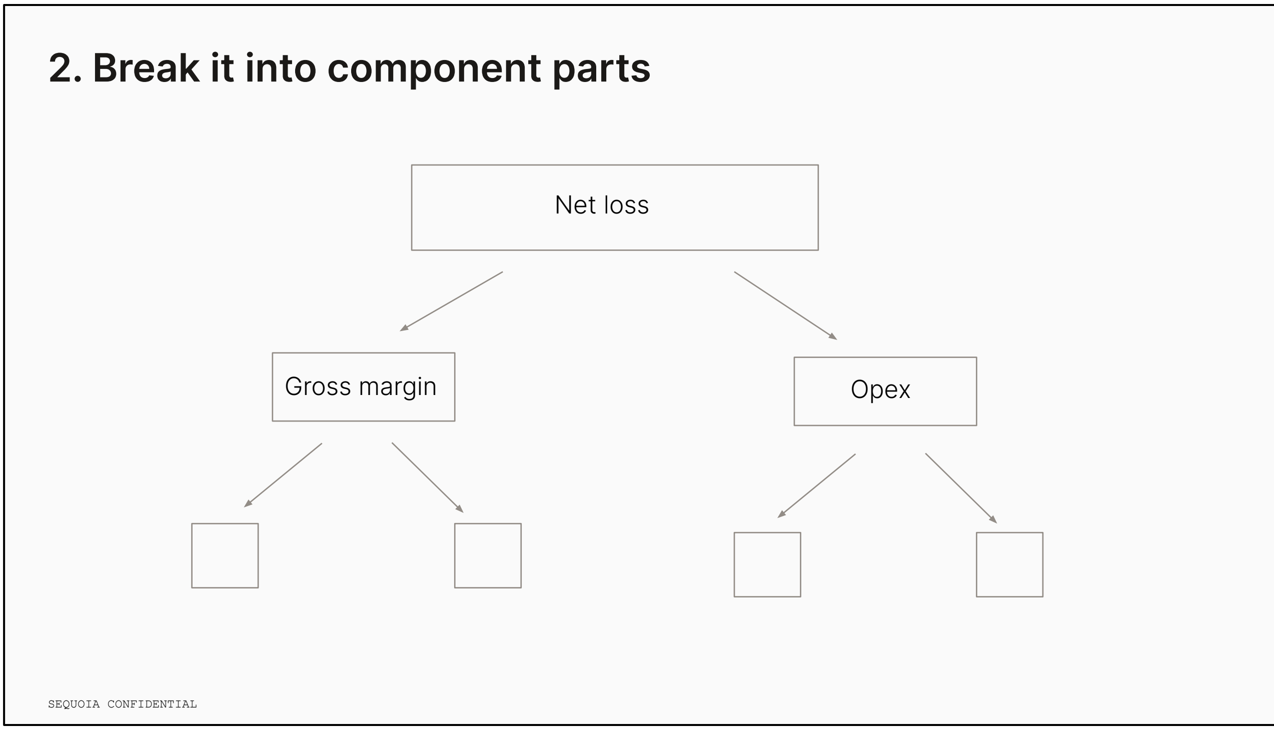
- Where does your net loss come from?
- Break it into smaller and smaller parts

Do the same exercise for cash items that don’t show up on the P&L

Understand what spend is efficient vs inefficient

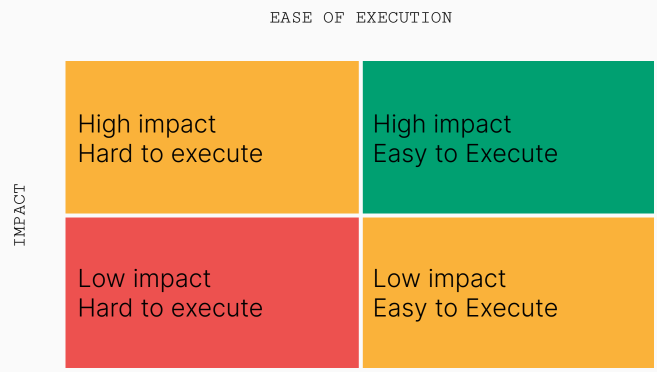


- The first step in getting very tactical is to understand your current state.
- This means looking deeply into your P&L. If you're talking about runway, that means you're losing money every month. So you have to figure out where the net loss comes from.
- Once you’ve identified the specific places in your P&L causing your burn, you can start thinking about which dollars yield efficient growth and which are not as helpful.



- To understand which parts of your P&L need to be addressed, begin with the big picture and break it down into component parts.
- Starting with net loss, you can break that into two component parts: gross margin and opex.
- Then break each of those down into component parts:
  - What are all the drivers of your gross margin? What is the cost of sales, etc?
  - What are all the drivers of compensation opex and non-compensation opex? How much of the opex is dedicated to computer hardware, hosting and subscriptions, etc?
- Keep breaking it down until you have a detailed view of the components that contribute to total net loss.

3. Lay out the potential changes you could make based on potential burn impact and ease of execution



- Once you've identified the important contributions to your burn, you can plot them in terms of their burn impact on the y-axis.
- Then there's ease of execution: how easy is it to address and how big an impact doe it have?
- Unfortunately, you're not likely to find many items that are high impact and easy to execute. Changes that extend your runway a lot will almost certainly be difficult.
- This plot is important because it will set your roadmap for the actions you take to extend your runway.

4. Set a goal

Your goal = Extending runway from current levels to a level where you can reach **a rational milestone**

(flat round fundraise, up round or cash flow positive)

- Once you understand the levers available to impact runway, you can use them to set a goal. Your goal should be oriented around how long it’s going to take for you to reach a rational milestone.
- Let's say your goal is a flat round. Given the market conditions, for many of us that’s going to take us three years.
- To unpack why that is:
    - Say you hypothetically raised your last round at a billion dollars, and you have five to 10 million of ARR.
    - We think that if you want to raise your next round at a billion dollars, you might need 75 to 100 million of ARR, which might mean you need to grow about 10 to 15X.
- It takes time to do that. It very well might take three or four years.

4. Set a goal

(Your goal) + 12

- If it takes three years, we recommend you have four years of runway.
- The reason: as mentioned earlier in the presentation, you want to raise 12 months before running out of money.
- Generally investors view it as a bad sign to have a very short runway, so you want to avoid being in this situation when raising a round.
- So the time you need to hit your goal plus 12 months is the ideal runway that we would suggest.
- One recommendation: When you decide how long it will take to reach your goal, be very realistic. Use public comps and ask the toughest board member. Ask her what it will take to reach a flat round based on rational milestones, and then add 12 months.

5. Execute on this goal

It's going to be hard

People-related cuts

Pricing increases

It gets better

Increased ownership and motivation

Sales efficiency

Extended runway

- So now you've taken the steps to understand where you are, and you've broken down your P&L to understand where the money goes. You've plotted your options in terms of ease-to-execute versus burn impact. And you've set a goal based on rational milestones.
- So let's say hypothetically you need to cut your burn from $3 million a month to $2 million.
- We don't want to sugarcoat this: It's going to be hard.
- Of course a people-related cut is the hardest decision any leader makes. Beyond this, you may face many challenging and nuanced decisions:
  - If you're a global company, you might need to reevaluate certain markets.
  - If you're a company that's relied on a marketing or sales investment in order to grow, you might have to reevaluate your strategy.
  - You might have to increase pricing. This is scary, especially if you don't have time to fully test the value proposition.

- The big thing to remember is this: If you take the steps necessary to extend your runway in line with rational milestones, we are confident you and your whole company will be better on the other side.

Key Takeaways

You need a lot more runway than you think

You are what your P&L says you are - you need real metrics to raise your next round

Figure out your bucket, most of you are in bucket 2

It’s time to execute - take the steps to reduce burn and extend your runway!

- To conclude with a few key messages:
  - You likely need more runway than you think.
  - Ultimately, your next round will be based on your metrics, which is going to be reflected in your financials.
  - Be real about what bucket you're in. We think most companies are in Bucket 2, which is more than 12 months of cash, but needing to make some changes.
  - You have what you need to win. You have the ability to execute and we're here to help you in doing that.

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